

TOBACCO SETTLEMENT REVENUE UPDATE

by Gary S. Olson, Director

The State of Michigan has now received its first three payments under terms of the master settlement agreement reached between 46 states and the five largest United States tobacco companies on November 23, 1998. This article provides an update on the tobacco settlement revenue received by the State of Michigan and estimates as to the amount of tobacco settlement revenue the State will receive over the next five fiscal years.

Under the terms of the master settlement agreement, the tobacco companies will be making two types of direct payments to the states during the first five fiscal years of the settlement agreement. The payments are referred to as initial payments and annual payments.

Initial Payments

The initial payments are to be made during the period fiscal year (FY) 1999-2000 through FY 2002-03. Before any adjustments, these initial payments to states will total \$12.7 billion. Michigan will receive approximately 4.352% of the national payment total. These initial payments are subject to a volume adjustment. This volume adjustment will reduce the payments based on a formula that measures changes in the United States sales of cigarettes of the manufacturers participating in the national settlement agreement.

Table 1 provides a summary of the Senate Fiscal Agency's estimates of the amount of settlement revenues that the State of Michigan will receive from these initial payments. These payments should total \$485.3 million and the final payment will be received by the State on January 10, 2003. To date, the State has received two initial payments of \$107.5 million and \$93.6 million.

Table 1

| TOBACCO SETTLEMENT REVENUE SUMMARY INITIAL PAYMENTS TO MICHIGAN | | | | |
|--|---------------------|---------------------------|--------------------------|-----------------------|
| (millions of dollars) | | | | |
| Fiscal Year | Payment Date | Michigan's Payment | Volume Adjustment | Actual Payment |
| 1999-2000 | 12-1-1999 | \$107.5 | 0.0 | \$107.5 |
| 1999-2000 | 1-10-2000 | 107.6 | (14.0) | 93.6 |
| 2000-2001 | 1-10-2001 | 110.8 | (16.6) | 94.2 |
| 2001-2002 | 1-10-2002 | 114.2 | (19.4) | 94.8 |
| 2002-2003 | 1-10-2003 | 117.6 | (22.3) | 95.3 |

Note: Assumes a 12.85% volume adjustment in FY 1999-2000 and a 2.0% increase in each year thereafter.

Source: Senate Fiscal Agency estimates

Annual Payments

The annual payments to the states continue indefinitely under the terms of the master settlement agreement. As long as the participating tobacco companies are selling cigarettes in the United States, these annual payments will continue. The annual payments to states are subject to several adjustments that will affect the actual level of payments to each state. First, an inflation adjustment is applied to offset the impact of inflation on future payments. Second, a volume adjustment, identical to the volume adjustment applied to the initial payments, is factored in. Finally, a series of other adjustments, including nonparticipating manufacturer adjustments, is factored in, leading to the final payments to each state. Table 2 provides a

summary of the Senate Fiscal Agency estimates of the amount of settlement revenues that the State of Michigan will receive from the annual payments through FY 2004-05. Over the first six years of the settlement agreement, these annual payments to Michigan should total \$1.4 billion. To date, the State has received its first annual payment of \$150.5 million.

Table 2

| TOBACCO SETTLEMENT REVENUE SUMMARY ANNUAL PAYMENTS TO MICHIGAN (millions of dollars) | | | | | | |
|--|---------------------|---------------------------|-----------------------------|--------------------------|--------------------------|-----------------------|
| Fiscal Year | Payment Date | Michigan's Payment | Inflation Adjustment | Volume Adjustment | Other Adjustments | Actual Payment |
| 1999-2000 | 4-15-2000 | \$173.9 | \$ 5.9 | \$ (25.9) | \$ (3.4) | \$150.5 |
| 2000-2001 | 4-15-2001 | 193.2 | 13.3 | (34.6) | 1.3 | 173.2 |
| 2001-2002 | 4-15-2002 | 251.0 | 26.2 | (52.5) | 1.7 | 226.4 |
| 2002-2003 | 4-15-2003 | 250.8 | 35.5 | (60.5) | 1.7 | 227.5 |
| 2003-2004 | 4-15-2004 | 308.5 | 55.5 | (84.8) | 2.1 | 281.3 |
| 2004-2005 | 4-15-2005 | 308.3 | 67.6 | (95.6) | 2.1 | 282.4 |
| Note: Assumes a 3.0% inflation adjustment and a 12.85% volume adjustment in FY 1999-2000 and a 2.0% increase in each year thereafter. | | | | | | |

Tobacco Settlement Revenue Distributions

Table 3 provides a summary of the total tobacco settlement payments and the distribution of these payments once received by the State. Public Act 94 of 1999 provides that certain percentages of the total tobacco settlement payments are earmarked to the Merit Award Trust Fund.

Pursuant to provisions contained in Senate Bill 882, currently pending before the House Appropriations Committee, the balance of the total tobacco settlement revenues will be earmarked to the Tobacco Settlement Trust Fund. The actual expenditure of tobacco settlement revenues from either of the two trust funds will occur only following appropriations made by the Legislature.

Source: Senate Fiscal Agency

Table 3

| TOBACCO SETTLEMENT REVENUE SUMMARY DISTRIBUTION OF PAYMENTS TO MICHIGAN (dollars in millions) | | | | | |
|---|-----------------------------------|--|----------------------|--------------------------------------|----------------------|
| Fiscal Year | Tobacco Settlement Revenue | Earmarking of Revenue | | | |
| | | Michigan Merit Award Trust Fund | | Tobacco Settlement Trust Fund | |
| | | Percent Share | Dollar Amount | Percent Share | Dollar Amount |
| 1999-2000 | \$351.6 | 30.0% | \$105.5 | 70.0% | \$246.1 |
| 2000-01 | 267.4 | 50.0% | 133.7 | 50.0% | 133.7 |
| 2001-02 | 321.2 | 75.0% | 240.9 | 25.0% | 80.3 |
| 2002-03 | 322.8 | 75.0% | 242.1 | 25.0% | 80.7 |
| 2003-04 | 281.3 | 75.0% | 211.0 | 25.0% | 70.3 |
| 2004-05 | 282.4 | 75.0% | 211.8 | 25.0% | 70.6 |

Source: Senate Fiscal Agency estimates